

## **A mandated study of payment rates, payment areas, and risk adjustment for MA local plans**

**ISSUE:** The MMA directs MedPAC to complete a report that addresses three questions related to the payment system for MA local plans. What factors underlie the geographic variation in AAPCCs? What is the appropriate payment area for local plans? How well does the CMS-HCC, the risk adjustment system that CMS began using in 2004, predict beneficiaries' costs? This brief contains our analysis of these questions.

**KEY POINTS:** AAPCCs vary widely among counties. This variation is a concern because the MMA makes payments to local plans more reliant on AAPCCs. Previous use of AAPCCs resulted in perceptions of inequity. Beneficiaries in counties with high rates typically had more plans to choose from and were offered more comprehensive benefits.

We identified how much of the variation in AAPCCs is due to county-level differences in the price of inputs and special payments to hospitals in the form of IME, GME, and DSH. The remainder is attributable to providers' practice patterns, beneficiaries' preferences for care, and mix of providers.

Counties—the current payment area—often have large annual changes in AAPCCs and adjacent counties often have very different payment rates. Both these issues could be addressed with a larger payment area. We considered three alternatives to counties—all using the county as the building block. It is clear that larger payment areas mitigate the problems presented by counties. However, care must be taken to avoid making payment areas so large that the cost of providing care varies widely within payment areas. In addition, payment areas should represent plan market areas as accurately as possible.

We compared the CMS-HCC to a model that is based on beneficiaries' demographic information and found that the CMS-HCC predicts costs much better both for beneficiaries in good health and those in poor health. This indicates the CMS-HCC reduces advantages that result from attracting favorable risks.

**ACTION:** At this meeting, staff seek the Commissioners' feedback on draft recommendations.

**STAFF CONTACT:** Dan Zabinski (202-220-3722) and Scott Harrison (202-220-3739).